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In The
Supreme Court of the United States

OCTOBER TERM, 1992

ARKLA, INC., ...PETITIONER,

V.

JAMES C. PLEDGER, DIRECTOR, DEPARTMENT OF FINANCE AND ADMINISTRATION, STATE OF ARKANSAS, ...RESPONDENT.

RESPONDENT'S BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE SUPREME COURT OF ARKANSAS

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RESPONDENT'S BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE SUPREME COURT OF ARKANSAS

Respondent respectfully requests that this Court deny Petitioner's petition for writ of certiorari seeking review of the opinion of the Arkansas Supreme Court.

REASONS FOR DENYING THE WRIT

I.

THE DECISION OF THE ARKANSAS SUPREME COURT DOES NOT CONFLICT WITH ANY DECISIONS OF THIS COURT

Arkla Inc., Petitioner, is a Delaware corporation which has its principal places of business in Little Rock, Arkansas and Shreveport, Louisiana. During the period of January 1, 1976 through February 28, 1987, Petitioner was engaged in the business of producing, buying, transporting and selling natural gas in Arkansas, Louisiana, Kansas, Oklahoma, and Texas. Petitioner bought gas and transported it through its interstate transmission pipelines. Located throughout Petitioner's interstate pipeline system were "pumping stations". Three of the pumping stations were located in Arkansas (Dunn, Beirne and Taylor Stations). The pumping stations housed several compressors which were used to compress the natural gas in the pipeline to expedite its transportation. The compressors as well as the compressor station heating systems were fueled by natural gas which was withdrawn from the Petitioner's pipeline. (R. 243).

The pumping stations received natural gas in unknown proportions from Arkansas and the Anadarko and Arkoma basins located principally in Texas and Oklahoma. (R. 298, 300-301) The natural gas which remained in the pipeline was transported further into Arkansas or on to Missouri, Louisiana or Texas. (R. 262-263 and 275).

The Respondent assessed the Petitioner Arkansas gross receipts (sales) tax on the value of the natural gas which was withdrawn from the pipeline to fuel the pumping stations. The Petitioner asserted that the Respondent's assessment was barred by the Commerce Clause. The Arkansas Supreme Court upheld the tax assessment.

The sale of natural gas is a taxable transaction in the State of Arkansas. Ark. Code Ann. §26-52-301. A sale is defined as the transfer of either title or possession of tangible personal property. The sales tax applies to the gross receipts or gross proceeds of the sale. Gross receipts or gross proceeds means the total amount of consideration for the sale including the value of any goods, wares, merchandise or property withdrawn or used from the established business or from the stock in trade of the established reserves for consumption or use in such business or by any other person. Ark. Code Ann. §26-52-103.

The Arkansas Supreme Court properly held that the State sales tax did not violate the Commerce Clause and applied the test outlined in *Complete Auto Transit v. Brady*, 430 U.S. 274, 51 L.Ed.2d 326, 97 S.Ct. 1076 (1977). The Arkansas Supreme Court followed previous Arkansas court decisions which found this type of transaction to be taxable. *Georgia Pacific Corp. v. Larey*, 242 Ark. 428, 413 S.W.2d 868 (1967); *Department of Public Utilities v. Arkansas Louisiana Gas Company*, 194 Ark. 354, 108 S.W.2d 586 *affirmed Arkansas Louisiana Gas Company v. Department of Public Utilities*, 304 U.S. 61, 58 S.Ct. 770, 83 L.Ed. 1149

(1937); *Southern Kraft Corporation v. Hardin*, 205 Ark. 512, 169 S.W.2d 637 (1943); *Arkansas Louisiana Gas Company v. Hardin*, 206 Ark. 593, 176 S.W.2d 903 (1944).

A. Conflicts Among the Supreme Courts of Several States.

The Petitioner claims that there is conflict among the states as to the taxation of this transaction. There is no conflict. Petitioner has cited *Midwestern Gas Transmission Co. v. Wisconsin Dept. of Rev.*, 84 Wis.2d 261, 267 N.W.2d 253 (1978) to support its statement. *Midwestern* is a Wisconsin use tax case which held that natural gas that was used in Wisconsin to fuel compressor stations had never come to rest in the state and therefore was not taxable under the Wisconsin use tax statute. The Wisconsin Court found that none of the gas had been produced in Wisconsin and that in order to sustain a use tax assessment, the item taxed must "come to rest" in the state. The facts presented by Petitioner differ in such a substantial manner so as to resolve conflict which may be seen to arise from the Wisconsin Court's decision in *Midwestern*. First, the gas in the Wisconsin case was produced outside the taxing state and, for the most part, would be shipped to points outside Wisconsin. In the present case, a portion of the gas which was being shipped by Petitioner had been produced in Arkansas and would be consumed Arkansas. Petitioner is unable to establish the amount of natural gas which is produced outside of Arkansas to draw itself closer to the facts in the *Midwestern* case. The Petitioner's constitutional question, without specific evidence of interstate commerce, would amount

to nothing more than giving an advisory opinion on an abstract, hypothetical legal question.

Assuming *arguendo* that all facts relating to gas production and use were identical and the tax statutes in the present case and the *Midwestern* case were similar (i.e. both use tax or both sales tax) Petitioner's argument that this Court should follow the *Midwestern* case is not controlling because of the Petitioner's substantial nexus with the State of Arkansas. The taxpayer in *Midwestern* did not have the ties to Wisconsin to allow the imposition of the tax as does Arkla. Therefore, the *Midwestern* case can be distinguished upon its facts.

In a later Wisconsin case, *Wisconsin Tel. Co. v. Wisconsin Dept. of Rev.*, 125 Wis. 339, 371 N.W.2d 825 (1985), under the Wisconsin sales tax law, the Wisconsin court implied that it would have upheld a sales tax assessment upon the use of natural gas. In this case, the Wisconsin Supreme Court upheld a sales tax assessment on telephone calls which originated in Wisconsin and were billed to Wisconsin telephones. The court applied the *Complete Auto Transit v. Brady* standard and stated that the tax did not burden interstate commerce because there was no double taxation and that interstate and intrastate commerce were placed on equal footing. The court distinguished the *Midwestern* case and ruled consistently with the Arkansas Supreme Court, thereby resolving any conflict between the Arkansas and Wisconsin courts which may have seemed to exist.

The most recent cases involving the issue of taxation of compressor fuel are from the states of Mississippi[1] and Utah[2]. In both states, a combined sales and use tax was assessed on the consumption of compressor fuel withdrawn from an interstate natural gas pipeline. In both cases the courts applied the test of internal and external consistency. The tax was found to be internally consistent because every state could impose an identical tax and no multiple taxation would result. External consistency was met because the state had taxed only that portion of the revenues from the interstate activity which reasonably reflected the in-state component of the activity being taxed. Therefore, the Petitioner's argument that there is conflict among the State court decisions on this issue is incorrect. Each state court applied the proper standard of review, thereby negating the appearance of conflict.

The Supreme Court of North Dakota has also been consistent with the Arkansas Supreme Court on the issue of taxation of the fuel withdrawn from a pipeline system and consumed by the processing facilities. In *Rocky Mountain Oil & Gas Ass'n. v. Conrad*, 405 N.W.2d 279 (N.D. 1987), the North Dakota Supreme Court found that these transactions were taxable and that the burden upon interstate commerce was unsubstantiated.

Petitioner also asserts there is conflict in decisions

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[1]*Tennessee Gas Pipeline Co. v. Marx*, 594 So.2d 615 (Miss. 1992)

[2]*Questar Pipeline Co. v. Utah State Tax Commission*, 817 P.2d 316 (Utah 1991)

between the Supreme Courts of Tennessee and Arkansas. In the Tennessee case of *Texas Gas Transmission Corp. v. Benson*, 444 S.W. 2d 137 (Tenn. 1969) on very similar facts, the Tennessee Supreme Court struck down a use tax assessment upon natural gas consumption stating that the fuel "never came to rest" within the state before it was consumed. Therefore, no "taxable moment" existed under the Tennessee use tax statute. The Tennessee court relied upon *Helson v. Commonwealth*, 279 U.S. 245, 73 L.Ed. 683, 49 S.Ct. 279 (1929) and broadly construed the ban on taxation of interstate commerce to include any necessary and integral part of the interstate operation.

The decision of the Tennessee Supreme Court and the Arkansas Supreme Court do appear to conflict as to the standard to be applied in the taxation of compressor fuel. However, *Texas Gas Transmission* was decided in 1969 and based upon the standard of review of *Helson*, the *Complete Auto Transit* decision rendered by this Court in 1977 changed the perspective from which this Court views taxing statutes.

Looking beyond the formal language of the tax statute to its practical effect and applying the test outlined in *Complete Auto Transit*, does the tax assessed in either the Tennessee case or the present case violate the Commerce Clause? The answer is no. There is no threat of double taxation. The fuel is consumed and will never be taxed again. The Petitioner is unable to show that the natural gas withdrawn from the pipeline was previously subject to tax in another state. Where is the burden upon the interstate operation? The Petitioner is unable to establish the percentage of

natural gas which is produced within and without Arkansas and the percentage of the gas which will eventually be used in Arkansas or shipped to another state. Therefore, a portion of the gas which is withdrawn from the pipeline and consumed is intrastate gas. Petitioner is unable to show that the burden of taxation was borne by interstate gas to a greater extent than the intrastate gas. The tax is borne equally by the intrastate and interstate gas with the interstate gas not being subjected to multiple or double taxation.

In summary, the cases from Tennessee and Wisconsin can be distinguished from this case and present no real harm from minor conflict. If this Court chooses to reverse the Arkansas Supreme Court in this matter, a quagmire would result. The expectations and assessments of North Dakota, Wisconsin, Mississippi, Utah and Arkansas would be left undecided and in turmoil. Therefore, Respondent states that the decisions of the Arkansas Supreme Court do not significantly conflict with decisions of other state Courts. Therefore, the Petition for Writ of Certiorari should be denied.

B. Conflicts among the U. S. Supreme Court decisions and the decision of the Arkansas Supreme Court.

The Petitioner attempts to create an inconsistency between several U.S. Supreme Court cases and the decision of the Arkansas Supreme Court. Examining each case individually, there is no conflict with the decision of the Arkansas Supreme Court.

First, the Petitioner points to the case of *McLeod v. J. E. Dilworth Co.*, 322 U.S. 327, 88 L.Ed. 1304, 64 S.Ct. 1023 (1944) to support its proposition that neither a sales nor a use tax can be assessed upon the use of this fuel. The Respondent does not disagree that the State of Arkansas may not assess a sales tax upon interstate sales which both originated and are completed in another state, but those are not the facts before this Court. A portion of the gas consumed as fuel by the Arkansas compressors was produced in Arkansas. Therefore, the "sale", as defined by Arkansas law, occurred in Arkansas and the authority to assess sales tax arose. *Department of Public Utilities v. Arkansas Louisiana Gas Company*, 194 Ark. 354, 108 S.W.2d 586 *affirmed Arkansas Louisiana Gas Company v. Department of Public Utilities*, 304 U.S. 61, 58 S.Ct. 770, 83 L.Ed. 1149 (1937); *Southern Kraft Corporation v. Hardin*, 205 Ark. 512, 169 S.W.2d 637 (1943); *Arkansas Louisiana Gas Company v. Hardin*, 206 Ark. 593, 176 S.W.2d 903 (1944).

Petitioner also cites *Helson & Randolph v. Kentucky*, 279 U.S. 245, 73 L.Ed. 783, 49 S.Ct. 279 (1929) as controlling authority of the U. S. Supreme Court which conflicts with the decision of the Arkansas Supreme Court. In *Helson* a use tax upon gasoline used to power a ferry was struck down. The Court held that the tax is exacted as the price of the privilege of using an instrumentality of interstate commerce. Disregarding the sales/use tax distinction and comparing the ferry boat to the compressor, there appears to be conflict between the decisions. The *Helson* decision was rendered in 1929 and this Court, in its recent decisions, has taken a practical and more realistic approach to

whether a tax is a burden on interstate commerce. The standard of review has moved from the broad and superficial examination applied in *Helson* which looked to whether the tax applied to anything which moved in interstate commerce to the indepth and realistic approach applied in *Complete Auto Transit* which looks to whether there is double taxation of interstate commerce and whether the tax is related to benefits received by the taxpayer. *D.H. Holmes v. McNamara*, 486 U.S. 24 (1988); *Quill Corporation v. North Dakota*, 119 L.Ed.2d 91, 112 S.Ct. 1904 (1992).

Therefore, while the *Helson* case has not been specifically overruled, the law announced therein has ceased to be viable in the ever changing area of interstate commerce.

II.

THE DECISION OF THE ARKANSAS SUPREME COURT DOES NOT BURDEN INTERSTATE COMMERCE

The facts of this case do not present the issues raised by Petitioner. Petitioner argues that the sales tax assessed by Respondent is a direct tax upon a commodity in interstate commerce. The theory behind the tax restriction on interstate commerce is to prohibit double taxation and to allow goods to flow freely between the states. The tax levied herein does not violate either of these principals. The tax imposed upon the pipeline company is not a direct tax and does not violate the Commerce Clause. The activity taxed, the consumption of natural gas in compressor stations located in Arkansas, has a sufficient nexus with the State to justify the tax. The tax is fairly apportioned to assess only local activities and does not discriminate against interstate commerce by subjecting interstate taxpayers to a double taxation where similarly situated intrastate taxpayers would only be subject to single taxation. Finally, the tax is fairly related to the benefits provided by the State to the pipeline company. *Complete Auto Transit Inc. v. Brady*, 430 U.S. 274. 51 L.Ed.2d 326, 97 S.Ct. 1076 (1977). The Petitioner has not presented facts which establish double taxation or a burden on interstate commerce.

CONCLUSION

For the reasons stated above, this Court should deny Petitioner's Petition for Writ of Certiorari.

Respectfully submitted,

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